

UNITED STATES OF AMERICA  
POSTAL REGULATORY COMMISSION  
WASHINGTON, DC 20268-0001

Competitive Product Prices  
Parcel Select  
Parcel Select Contract 24

Docket No. MC2018-13

Competitive Product Prices  
Parcel Select Contract 24 (MC2018-13)  
Negotiated Service Agreement

Docket No. CP2018-26

PUBLIC REPRESENTATIVE COMMENTS ON  
POSTAL SERVICE REQUEST TO ADD PARCEL SELECT CONTRACT 24 TO THE  
COMPETITIVE PRODUCT LIST

(October 26, 2017)

**I. Introduction**

The Public Representative hereby provides comments pursuant to the Commission Notice initiating this docket.<sup>1</sup> In that Notice, the Commission established the above referenced docket to receive comments from interested persons, including the undersigned Public Representative, on the Postal Service's request to add Parcel Select Contract 24 to the competitive product list.<sup>2</sup>

Under 39 U.S.C. § 3642(b) the criteria governing Commission review are whether the product (1) qualifies as market dominant, (2) is covered by the postal monopoly and therefore precluded from classification as a competitive product, and (3) reflects certain market considerations, including private sector competition, the impact on small businesses, and the views of product users.

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<sup>1</sup> PRC Notice Initiating Docket(s) for Recent Postal Service Negotiated Service Agreement Filings, October 19, 2017 (Notice).

<sup>2</sup> Request of the United States Postal Service to Add Parcel Select Contract 24 to Competitive Product List and Notice of Filing (Under Seal) of Unredacted Governors' Decision, Contract, and Supporting Data, October 18, 2017 (Request). On October 23, 2017, the Postal Service filed revised financial workpapers. United States Postal Service Notice of Filing Revised Financial Workpapers, Including Material Under Seal (Errata), October 23, 2017.

Under 39 U.S.C. § 3633(a), competitive products must not subsidize market dominant products; each competitive product must cover its attributable costs; and all competitive products must collectively contribute an appropriate share of the institutional costs of the Postal Service.

## **II. Comments**

The Public Representative has reviewed the Postal Service's Request, Statement of Supporting Justification, attached contract, Certification of Compliance with 39 U.S.C. § 3633(a), and proposed revised changes to the Mail Classification Schedule (MCS). The Public Representative has also reviewed the supporting financial models for the contract filed separately under seal.

### **a. Analysis of the Nature of the Agreement and its Classification**

The Postal Service states that Parcel Select Contract 24 is "modeled off of the Customized Delivery market test, which is scheduled to expire on October 31, 2017."<sup>3</sup> In approving an exemption from the market test's annual revenue limitation, the Commission stated that "In addition, if the Postal Service files a request to add Customized Delivery as a permanent product, data collection reports must be complete to ensure the Commission has sufficient time to evaluate the request before the market test expires."<sup>4</sup>

The Commission also stated that "[i]f the Postal Service decides to add Customized Delivery as a permanent product, it must file a request for permanent product status under 39 C.F.R. § 3035.18 at least 60 days before the market test expires. See 39 C.F.R. § 3035.18(a). Because the market test expires on October 31, 2017, the Postal Service must file the request by September 1, 2017." *Id.* While the instant agreement does not constitute a permanent product, because it has a proposed term of three years<sup>5</sup>, the process by which the Postal Service has developed this

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<sup>3</sup> Request at 1. See Docket No. MT2014-1, Order Authorizing Extension of Customized Delivery Market Test and Updating Data Collection Plan, September 28, 2016.

<sup>4</sup> Docket No. MT2014-1, Order Approving Request for Exemption, May 18, 2017, at 10 (Order No. 3905).

<sup>5</sup> Request, Attachment B at 5.

agreement, and the incompleteness of the prior data collection reports, fail to achieve the spirit of transparency intended by Order No. 3905.<sup>6</sup>

The Postal Service makes a number of assertions that address the requirements of section 3642(b). See Request, Attachment D. These assertions are reasonable. Additionally, because the initial market test was classified as competitive, and appropriately justified as such<sup>7</sup>, the Public Representative concludes that this agreement satisfies the criteria of section 3642(b), concerning the classification of new competitive products.

### **b. Analysis of the Financial Model**

This agreement is based on the Customized Delivery market test. As a result, the Postal Service presents a new cost model unique to this agreement. The Public Representative agrees with the Postal Service's use of a new cost model given the unique nature of this agreement.

The cost model itself, however, is untested, relying on limited data and questionable assumptions. In city and rural non-Hub delivery, both the "Dedicated Cost" and "Dedicated %" estimates are based on "PTR Scans of FY17 Q3 customized delivery packages."<sup>8</sup> These costs are reliant on a relatively new system, the Product Tracking and Reporting System (PTR). While the Postal Service asserts that this system is potentially reliable for developing cost estimates, the Commission has not yet formally approved its use in cost estimation.<sup>9</sup> Additionally, the PTR data are based solely on one quarter of data (Q3 Packages), whereas the costing methodologies used in the Cost And Revenue Analysis report are based on four quarters of data. The Public Representative is concerned that the limited amount of observations could result in volatile cost estimates, particularly if this product exhibits seasonal variability in volume.

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<sup>6</sup> The Postal Service states that the complexity of the Customized Delivery contract prevented an earlier filing and commits to providing prompt responses to any information requests. Request at 1, n.1 (and accompanying text).

<sup>7</sup> See Docket No. MT2014-1, Order No. 2224 at 14.

<sup>8</sup> "PS24\_Analysis.Revised.10.23.Public.xlsx," tab "PartnerUnitCosts," cell A51.

<sup>9</sup> See Docket No. PI2017-1, Response to CHIR No. 1, Question 1; See also Docket No. RM2015-7, USPS Response to Order 2792, at 6-9.

Moreover, *all* of the Hub delivery costs are based on the “Customized Delivery FY17 Q3 Report.”<sup>10</sup> Once again, the Postal Service is relying on just one quarter of data for annual costs of a type of delivery. Depending on the magnitude of DDU Hub deliveries, any volatility in this cost estimate may have a disproportionate impact on cost coverage.

Several of the parameters used in estimating transportation costs, particularly “SCF-DDU Miles” and “Utilization,” are based on assumptions.<sup>11</sup> The Public Representative expresses similar concerns with these assumptions as those stated above.

Although the Public Representative has concerns with the cost estimates, the negotiated prices should generate sufficient revenues to cover costs during the first year of the contract, and therefore comply with the requirements of 39 U.S.C. § 3633(a), to the extent that the cost estimates are reliable and accurate. Given these concerns, the Public Representative recommends the Commission require timely<sup>12</sup> and complete quarterly data reports on the volumes, costs, and revenues of this agreement. These reports should be similar in form to the model provided in the instant docket. In these reports, the parameters of the cost model should be updated with additional data accurately reflecting on the performance of this agreement.<sup>13</sup>

The contract is expected to remain in effect for a period of three years. The Postal Service provides no evidence to demonstrate that the contract will comply with the requirements of 39 U.S.C. § 3633(a) during the second and third years of the contract. Given this cost model is unique to this agreement and relies upon limited data, it is likely the cost estimates will have a large variance. This concern is not mitigated by the annual adjustment in the contract prices. The Public Representative cannot recommend approving this agreement beyond the first year without more accurate cost data. He therefore recommends that the Commission review the performance of this

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<sup>10</sup> “PS24\_Analysis.Revised.10.23.Public.xlsx,” tab “PartnerUnitCosts,” cell A57.

<sup>11</sup> *Id.* at cell A58.

<sup>12</sup> No less than 30 days after the end of a contract quarter.

<sup>13</sup> This reporting is not without precedent for agreements based on market tests. See Docket No. CP2016-50, Order Adding Priority Mail Contract 167 to the Competitive Product List.

agreement after one year to assess whether it should be renewed, modified, or terminated.

Finally, the Commission has an opportunity to conduct an annual compliance review in its Annual Compliance Determination. The Public Representative encourages the Commission to track this contract as quarterly data reports are provided.

### **III. Conclusion**

The Public Representative therefore recommends the following:

1. The Commission approve this agreement for a duration of one (1) year.
2. The Commission require timely and complete quarterly data reports on the volumes, costs, and revenues of this agreement, in the form provided in the instant docket, in which the parameters of the cost model will be updated with data based on the performance of this agreement.
3. The Commission review the performance of this agreement after one year to assess whether it should be renewed, modified, or terminated.

The Public Representative respectfully submits the foregoing comments for the Commission's consideration.

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